CANADA

Prices and incomes commission

Commission des prix et des revenus

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COFFEE PRICES

Prices and Incomes Commission

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FOREWORD

The Prices and Incomes Commission was established on June 19, 1969, "to inquire into and report upon the causes, processes and consequences of inflation and to inform those making current price and income decisions, the general public and the Government on how price stability may best be achieved".

Following numerous separate discussions with representatives of the Canadian business community, including the Canadian Chamber of Commerce, the Canadian Manufacturers' Association, the Retail Council of Canada and the Canadian Bankers' Association, the Commission decided to call a National Conference on Price Stability in order to obtain a consensus on a national policy to combat inflation. The conference, held in Ottawa on Feb. 9-10, was attended by senior officers of national business and farm associations, representatives of professional groups, leaders of the Canadian business community and officials of the federal and provincial governments. Those present indicated a willingness to exercise a meaningful degree of restraint in their pricing policies in 1970 and there was broad agreement that:

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(a) Business firms generally, if called upon to do so, would reduce the number and size of price increases they would normally make in 1970.

(b) More specifically, where higher prices are needed to cover higher costs, and market conditions make them feasible, business firms generally, if called upon to do so, would ensure that price increases were clearly less than the amount needed to cover the increases in costs at a normal volume of output and sales.

The complete list of agreed criteria is contained in the Closing Statement of the National Conference on Price Stability released on Feb. 10, 1970.

At a Federal-Provincial Conference of First Ministers, held in Ottawa on Feb. 16-17, 1970, the federal government and all provincial governments endorsed the Commission's plan to call without delay upon business firms generally to follow the basic price restraint principle adopted by the National Conference on Price Stability. First Ministers urged all Canadians to co-operate actively in restraining price and income increases during 1970.

Provision was made at the National Conference on Price Stability for a price review procedure whereby the Prices and Incomes Commission would review price increases to determine whether they comply with the agreed criteria.

The Government of Canada and most provincial governments expressed the hope that government sanctions would not be required but agreed that if necessary they would use such means as are within their control to deal with cases of serious non-compliance with the pricing criteria as reported by the Commission.

INTRODUCTION

In April and May, 1970, several coffee processing companies announced an increase from \$0.95 to \$1.01 per pound in the wholesale price of ground, roasted coffees. On May 5, 1970, the Prices and Incomes Commission announced its intention to undertake a review of coffee prices to ensure that the increases comply with the criteria agreed at the National Conference on Price Stability.

The criteria are designed to be applied to the circumstances of individual companies which implement price increases. In accordance with the procedures proposed at the national conference, the Commission has obtained detailed information from four coffee-processing companies and has compiled and reviewed this information separately in order to determine the position of each company in relation to the criteria.

The criteria also stipulate that 1969, or the nearest fiscal year, will in general be used as the base year when considering changes in costs and revenues and that a suitable alternative base year would be selected only if 1969 would clearly be inappropriate. This point was reviewed with the companies concerned and it was agreed in all cases that 1969 constituted a suitable basis for comparison.

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Six companies produce the bulk of roasted and soluble coffee consumed in Canada. They are: Brooke Bond Foods Ltd., General Foods Ltd., Mother Parker's Foods Ltd., Nabob Foods Ltd., Nestlé (Canada) Ltd. and Standard Brands Ltd.

The price increase which initiated this review related to roasted coffee only; the wholesale price of soluble coffee has not been increased during 1970. Nabob Foods Ltd. has not increased wholesale coffee prices in 1970 and has been excluded from the review. Nestlé (Canada) Ltd. produces soluble coffee only and has not increased prices in 1970 but assisted the Commission by providing information for comparative purposes. Information on financial performance, markets, prices, revenues and costs were obtained from Nestlé and the other four companies.

Processed coffee is available in three principal forms: Roasted coffee (ground or as a roasted bean); spray-dried soluble coffee; and as freeze-dried soluble coffee. In the first form the coffee is ground, if necessary, and percolated by the consumer. In the second two forms hot water is added to make 'instant'

coffee. Current Canadian consumption of instant coffee runs at something under two-thirds of total consumption.

Table 1 shows Canadian imports, production and exports over the five years to December, 1969.

Canadian production of roasted and soluble coffees has remained fairly static over the five-year period, while imports of both roasted and soluble coffees have climbed. World green coffee consumption in importing countries has remained at around 6,900,000 pounds over the last five years. Canada's share of world imports is thus currently around 2.5 per cent.

Table 1

Canada Coffee Imports, Production and Exports
(Thousands of pounds)

	1965	1966	1967	1968	1969
Green coffee bean imports	166,357	153,917	177,751	184,441	180,244
Roasted coffee production	99,040	97,806	99,721	101,945	96,990
Soluble coffee production	18,975	20,362	19,754	21,966	23,665
Roasted coffee imports	2,642	3,476	4,194	4,955	5,437
Soluble coffee imports	2,146	2,601	3,114	4,711	5,751
Roasted coffee exports	nil	nil	nil	nil	nil
Soluble coffee exports	1,576	1,132	828	979	2,413

Price Increases

Price changes at the wholesale level by coffee processors usually correspond in size and timing. Table 2 shows the wholesale price history of leading brands of roasted, spray-dried soluble and freeze-dried soluble coffees over the years 1965 to date.

Processed coffee prices are volatile and correspond with changes in the price of green coffee. Over the last 15 years there have been more than 30 changes up and down in wholesale roasted coffee prices. Current wholesale prices are equivalent to those prevailing in the mid-1950's.

Table 2

Wholesale Coffee Prices 1965 to Date
(Canadian dollars per pound)

		Roasted Coffee	Spray-dried Soluble Coffee	Freeze-dried Soluble Coffee
1965	January	0.83	2.64	-
	March		2.54	
1967	February	0.79		
1968	April			3.80
	June		2.64	
	December	0.83		
1969	September	0.87	2.77	4.00
	October	0.91	2.91	4.12
	December	0.95		
1970	April	1.01		

Note: 1. Freeze-dried soluble coffee was introduced to the Canadian market early in 1968.

2. The prices quoted for the spray-dried and freeze-dried soluble coffees are for the 10-ounce and four-ounce jars respectively, adjusted to a dollars-per-pound price.

Costs

On average, green coffee costs form approximately 55 per cent of the sales value of roasted coffee. Direct labor costs amount to about 8 per cent and advertising and other marketing costs approximately 10 per cent. At the time of undertaking this review, the Commission noted that the price of green coffee in world markets has risen sharply. The composite monthly average price of green coffee moved from U.S. 36 cents per pound in January 1969 to U.S. 49 cents per pound in January 1970, an increase of 35 per cent over the twelve-month period. The composite price as at May 1970 was U.S. 51 cents.

Several reasons account for this sharp increase. During the 1960's the picture has changed from one of surplus coffee production in the first half of the decade to one of consumption exceeding production. The change has been obscured, to some extent, by the reduction of surplus stocks in Brazil. Brazil has had four bad harvests successively and its once massive surplus stocks are now much reduced to an estimated 30 million bags.

Brazil and other Latin-American countries currently supply about two-thirds of the world market compared with about three-quarters at the beginning of the

1960's. Africa's gain in the world market over this period almost accounts for Latin America's reduced share. Brazil, particularly, produces almost exclusively high grade Arabica coffee, a coffee which is in increasing demand. During July 1969 there was serious frost damage to the Brazilian coffee crop which had an immediate and dramatic effect on green coffee prices.

It is beyond the scope of this review to forecast future green coffee price trends. The Commission has consulted Canadian coffee processing companies and others familiar with the trade and the consensus is that a price fall is not imminent. World coffee stocks are considered to be low and news has recently been received of a coffee leaf disease, hitherto confined to African coffees, which threatens the Brazilian plantations. Green coffee production over the next several years is dependent on the present tree population. Most of the trees were planted before 1960 and have passed their peak.

If present green coffee and wholesale coffee prices remain constant for the balance of 1970, the increase in the cost of green coffee in 1970 over 1969 will exceed the increase in revenue derived from wholesale price increases, even after making allowance for the freeing of the Canadian dollar. In other words, coffee

processors are facing increments in green coffee costs alone which exceed revenue increases from the recent price adjustments.

The market in Canada for coffee has shown little or no growth in recent years. Competition from other beverages is intense. As a result, there is very considerable resistance to price increases. The coffee processors have thus found themselves in a severe cost/price squeeze. Of the firms examined, two appear likely to face losses in 1970, one may break even and the fourth firm will almost certainly realize reduced profits.

The rise in the price of green coffee beans has therefore had the unpleasant consequence for Canadian consumers of forcing prices upward. Because the great majority of adults consume this beverage, they are sensitive to price changes in this product.

The Canadian coffee processor is equally sensitive to price developments because he faces strong consumer resistance to price increase, and has been forced to absorb increased costs to a point where profits have been minimized or eliminated.

CONCLUSION

In the case of each of the four companies to which the criteria have been applied it is clear that increased costs of coffee alone have been greater than the additional revenues from price increases. For this reason the companies meet the criteria.